



## **OXFORD ANALYTICA**

### **MALAYSIA**

### **MONETARY TRANSPARENCY**

#### **Country Report 2005**

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5 Alfred Street  
Oxford OX1 4EH

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# MALAYSIA



## COMPLIANCE RATINGS

<i>Monetary transparency</i>	2005	2004	2003	2002
Clarity of roles	••••	••••	•••	••
Open decision process	••••	••••	•••	••
Availability of information	••••	••••	••••	••••
Accountability	••••	•••	•••	•••
<b>Score</b>	<b>4.00</b>	<b>3.75</b>	<b>3.25</b>	<b>2.75</b>

## OUTLOOK & COMMENTARY

Although Malaysia maintained a relatively independent interest rate regime -- thanks to limited access to ringgit offshore operations -- the reintroduction of a managed float for exchange rate policy should help Bank Negara Malaysia (BNM) gain efficiency in the conduct of monetary policy while providing greater clarity over policy implementation. A welcome development has been the launch in February 2005 of the BNM Laman Informasi Nasihat dan Khidmat (LINK), which aims to enhance the effectiveness of BNM's interface with the public.

Public consultations and comprehensive information services have strengthened BNM's accountability to the public by ratifying the integrity of its operations. Central bank officials have occasionally made statements in parliament and to the media to further clarify BNM's actions and decisions. In addition to its internal monitoring and oversight functions, BNM's Board Audit Committee works closely with the Auditor General to work on any recommendations for improvement in respect of, among other areas, risk management, governance and internal controls.

## EXECUTIVE SUMMARY

### 4.00 Compliance in progress

Bank Negara Malaysia (BNM) remains committed to improving public information services and overall monetary policy transparency. It issues press releases on its website announcing changes in monetary policy, the Overnight Policy Rate (OPR), and the range and settings of monetary instruments. These provide the rationale for changes and the time span for implementation. BNM officials regularly make statements about monetary policy in speeches, many of which can be found on the central bank's website.

Monetary statistics continue to meet the requirements of the IMF Special Data Dissemination Standard (SDDS), and the BNM has in place a structure of four main technical and informative publications to disseminate monetary policy information: the *Annual Report*, the *Quarterly Bulletin*, the *Monthly Statistical Bulletin*, and the *Monetary Policy Statement* that announces changes to the policy stance through the OPR. On 25 February 2005, the Bank Negara Malaysia Laman Informasi Nasihat dan Khidmat (LINK) was launched; its aim is to enhance the effectiveness of the BNM's interface with the public. Bank Negara Malaysia LINK is established as a centralised point of contact with the public on issues that relate to BNM's operations, policies, the financial sector and consumer education in the area of finance through face-to-face customer service to walk-in visitors with general enquiries or complaints.

On 21 July 2005, the exchange rate framework was moved to a managed float against a trade-weighted basket of currencies. The primary motivation for the shift in exchange rate policy was for Malaysia to be in the best position to deal with the structural changes occurring in the region. Under the managed float regime, the level of the ringgit exchange rate against other currencies, including the US dollar, is largely determined by market demand and supply. The BNM would only intervene to prevent excessive fluctuations in the value of the ringgit, and to ensure that the exchange rate does not depart significantly from the levels warranted by economic fundamentals.

The government's blanket guarantee for deposits has been replaced by an explicit, but limited, deposit insurance scheme, thus clarifying the BNM's facility of lender of last resort operations. Enacted on 15 August 2005, the Malaysia Deposit Insurance Corporation (MDIC) Act 2005 has established the Malaysia Deposit Insurance Corporation to administer the act and the country's deposit insurance scheme.

Malaysia's overall score has improved from 3.75 in 2004 to 4.00

## 1. CLARITY OF ROLES, RESPONSIBILITIES, AND OBJECTIVES OF CENTRAL BANKS



Compliance in progress

### The objectives and institutional framework of monetary policy

#### Central bank objectives and responsibilities

Malaysia's monetary policy framework is officially set out in the Central Bank of Malaysia Act 1958 (Revised 1994, CBA).<sup>1</sup> The legislation enumerates the principal objectives of the central bank, Bank Negara Malaysia (BNM), which are to issue currency and to keep reserves to safeguard the value of the currency, to act as a banker and financial adviser to the government, to promote monetary stability and a sound financial structure, and to influence the credit situation to Malaysia's advantage. The CBA was amended in 2003 to include additional objectives: to promote the reliable, efficient and smooth operation of national payment and settlement systems, and to ensure that the national payment and settlement systems policy is directed to the advantage of Malaysia. The CBA does not identify any priority between its objectives and provides little guidance on how to reconcile conflicting objectives. According to the central bank, its ultimate policy goal is economic growth and price stability.<sup>2</sup> The BNM has also highlighted its contributions to Malaysia's national development goals.<sup>3</sup>

The powers of the BNM are listed under Part V of the CBA. These include issuing currency, issuing securities, and accepting deposits. BNM powers relating to the supervision and regulation of the financial system are specified in Section 30 (3) of the CBA and specific powers are provided in the Islamic Banking Act 1983, the Takaful Act 1984, the Banking and Financial Institutions Act 1989, the Insurance Act 1963, the Development and Financial Institutions Act 2002, the Exchange Control Act 1953, the Money Changing Act 1998, and most recently the Payment Systems Act 2003, which came into effect in November 2003.<sup>4</sup> The BNM has also been appointed by the minister of finance as the competent authority to administer the Anti-Money Laundering Act 2001.

#### Operational autonomy

In 1998, after a public dispute with the prime minister over monetary policy, the governor of the central bank (Ahmad Don) and a deputy governor (Fong Weng Phak) resigned. Another official -- formerly in the Economic Planning Unit of the Prime Minister's Department -- then headed the bank temporarily and changed monetary policy to bring it in line with that proposed by then Prime Minister Dr. Mahathir Mohamad. In the past, commentators argued that the operational independence of the central bank was unclear since then, although recent developments in the conduct of monetary policy have highlighted the growing independence of the central bank under Prime Minister Abdullah Badawi.<sup>5</sup> The CBA establishes that the BNM Board of Directors shall keep the minister of finance informed of the monetary and banking policy; policies in respect of institutions in relation to which the central bank is conferred with powers under the Insurance Act 1963, the Islamic Banking Act 1983, the Takaful Act 1984, the Banking and Financial Institutions Act 1989 and the Money-Changing Act 1998; and policies in respect of the Exchange Control Act 1953, pursued or intended to be pursued by the central bank.

When disagreements arise, the CBA gives the minister of finance considerable weight over monetary policy decisions. According to Section 34, if the minister of finance disagrees with the BNM Board on any policies, the minister may "issue directives to the Board relating to such policies, and any such directive shall become binding on the Board, which shall forthwith take all steps necessary or expedient to give effect thereto."<sup>6</sup> If the Board objects to the minister's directive, it may submit its objections in writing to the minister of finance who is then obliged to

present those objections together with the minister's directive to the House of Representatives. To date, the BNM has never submitted objections in writing to the minister; differences in opinion have been "settled through other avenues".<sup>7</sup> The federal constitution vests the legislative authority of the country to the parliament, which consists of the Yang di-Pertuan Agong (the Supreme Ruler) and the two Houses of Parliament; any ruling of the parliament is binding on the MoF and the BNM.

The BNM has asserted that it conducts monetary policy in coordination with other government institutions and receives suggestions from the minister of finance. In this context, BNM officials have stressed that the central bank remains operationally autonomous.<sup>8</sup> For example, during the period when the prime minister publicly threatened to raise the statutory reserve requirement ratio to pressure commercial banks to increase lending and promote economic activity, the BNM made no changes to these requirements.<sup>9</sup>

## **Institutional relationship between monetary and fiscal operations**

### **Lending to government**

Section 33 of the CBA allows the BNM to grant temporary advances to the government, which cannot amount to more than 12.5% of the estimated government receipts for that financial year. These must be paid back no later than three months after the end of the financial year in which they were granted. The BNM is free to determine the interest rates of these advances. However, this provision has never been exercised.<sup>10</sup>

### **Central bank involvement in the rest of the economy**

The CBA allows the BNM to carry out various fiscal or quasi-fiscal activities, many of which have never been implemented. Section 30 of the CBA allows the setting up of a Special Investment Fund -- with the approval of the BNM board and the minister of finance -- for the purpose of economic development using funds from banking institutions' statutory reserve ratios. This fund cannot exceed the amount of the BNM's General Reserve Fund.<sup>11</sup> Subsection 30 (1) (h) and (j) of the CBA allows the BNM to purchase, sell, and hold securities of the Malaysian or state governments or public authority, and hold securities of corporations set up with government approval to develop financial markets. Subsection 30 (1) (o) empowers the BNM to purchase and sell securities issued or guaranteed by any foreign government or international financial institution.

At present, the BNM still owns about 79.3% of the Credit Guarantee Corporation's share capital. This firm was set up in 1972 to assist viable small- and medium-sized enterprises, particularly those without collateral or with inadequate collateral to obtain credit facilities from financial institutions by providing guarantee cover on such facilities.

The BNM also owns 20% of *Cagamas*, the national housing mortgage agency and a major supplier of domestic bonds. *Cagamas* bonds play a key benchmarking role for the local bond market, a market that the BNM's operating legislation encourages it to develop. A deputy governor of the BNM is chairman of *Cagamas*. For development purposes, the BNM issues broad lending guidelines to all banking institutions operating in Malaysia to ensure that certain economic sectors, deemed by the government to be of primary importance, have continuous access to credit. Such directed lending is extended based on commercial rates and terms.<sup>12</sup>

The procurement of services follows the central bank's *Purchasing Procedural and Authorisation Policies* (PPAP), which are internal administrative guidelines. These guidelines are consistent with the provisions of the CBA and the powers of the BNM Board as provided in the CBA.<sup>13</sup> There is currently a task force working on more comprehensive procurement procedures, which will be completed in the near term.<sup>14</sup>

### **Central bank profit allocation**

The CBA details conditions for the allocation of BNM profits. The amount to be placed in the General Reserve Fund (GRF) will be recommended by the BNM Board, and determined by the minister of finance after consultation with the BNM Board, and the remainder is paid to the government.<sup>15</sup> If at the end of the financial year the GRF is less than half the paid-up capital of the central bank, then all profits are transferred into the GRF. If the fund accumulates more than half (but less than twice) the paid-up capital then at least 30% of the net profit is transferred to the GRF.<sup>16</sup> By mid-2005, the BNM's GRF far exceeded its paid-up capital.

### **Agency roles performed by the central bank on behalf of the government**

The CBA designates the BNM as the banker and financial adviser to the government. The Development Financial Institutions Act 2002 brings six financial institutions for development, controlled by different agencies, under the scrutiny of the BNM. However, the central bank holds no equity stakes in any of these institutions. The BNM in its role as financial agent of the government regularly issues both conventional and Islamic treasury bills and bonds, under the Treasury Bills (Local) Act 1946 (Revised 1977), the Loan (Local) Act 1959 (Revised 2004), and the Government Funding Act of 1983.

## 2. OPEN PROCESS FOR FORMULATING AND REPORTING MONETARY POLICY DECISIONS

●●●● Compliance in progress

### The framework, instruments, and targets of monetary policy

#### Framework and monetary targets

The BNM's *Annual Report* provides a general description of monetary policy, and the CBA outlines monetary policy objectives from which targets can be derived. In the past, commentators had argued that the lack of clear and published annual targets substantially diminished monetary policy transparency.<sup>17</sup> In order to allay this concern, the BNM has stepped up its efforts to enhance transparency by improving its communication strategy and enhancing the dissemination of information to stakeholders.

The BNM uses interest rates as the main operating target. In April 2004, the BNM replaced the three-month Intervention Rate with the Overnight Policy Rate (OPR) as the main indicator of the monetary policy stance. The OPR has a dual role: as a signalling device to indicate the monetary policy stance and as a target rate for the day-to-day liquidity operations of the central bank.<sup>18</sup> Liquidity management is aimed at ensuring the appropriate level of liquidity that would influence the overnight inter-bank rate to move closer to the OPR. Liquidity operations are also conducted at other maturities without targeting a specific interest rate level, such that inter-bank interest rates at other maturities would be market determined -- reflecting overall demand and supply conditions in the money market as well as interest rate expectations. Any change in the OPR is announced in the *Monetary Policy Statement*, which is issued at predetermined quarterly intervals to coincide with the release of Malaysia's GDP data. Nevertheless, should there be a change in the monetary policy stance, in the period between two scheduled dates, an additional *Monetary Policy Statement* would be issued.<sup>19</sup>

The policy of non-internationalisation of the ringgit, adopted since the 1997-98 financial crisis and enforced through limiting access to ringgit offshore operations, has allowed Malaysia to set domestic interest rates while keeping the exchange rate stable. With regard to exchange rate policy, the BNM announced on 21 July 2005 the move to a managed float against a trade-weighted basket of currencies.<sup>20</sup> The primary motivation for the shift in exchange rate policy was to be in the best position to deal with the structural changes occurring in the region. Under the managed float regime, the level of the ringgit exchange rate against other currencies, including the US dollar, is largely determined by market demand and supply. The BNM would only intervene to prevent excessive fluctuations in the value of the ringgit, and to ensure that the exchange rate does not depart significantly from the levels warranted by economic fundamentals.<sup>21</sup>

#### Monetary instruments

The BNM is authorised to use a variety of instruments to pursue monetary policy, as outlined in Section 30 of the CBA. These include the purchase, sale and discount of government securities, foreign bonds, and currencies. Along with changes to interest rates and open market operations, the BNM regulates the statutory reserve ratio as a monetary policy instrument. The central bank provides the latest information on changes to monetary policy instruments in its press releases, *Monetary Policy Statement*, *Monthly Statistical Bulletin*, *Quarterly Bulletin*, and *Annual Report*. These are available on the BNM website. The BNM publicly discloses the rules and procedures for its relationship and transactions with counterparts mainly through its Circulars.

The CBA states that the exchange rate parity of the Malaysian ringgit is to be determined by the minister of finance with guidance from the BNM.<sup>22</sup> At present, however, the fixing of a parity for the ringgit is redundant in light of the move to a managed float regime. Nevertheless, Article 19 (4) of the CBA stipulates that the minister of finance may decide, on the recommendation of the BNM, that it is necessary and expedient for Malaysia not to determine an exchange rate parity for the ringgit, but instead to apply any exchange arrangement that is not inconsistent with the IMF Articles of Agreement. This includes, but is not limited to, the severing of the parity of the ringgit to any currency (or currencies) or a denominator.

## **The monetary policy-making body**

### **Monetary board**

Under the CBA, the BNM's Board of Directors is responsible for the strategy and general administration of the central bank's affairs and business -- it currently comprises four ex-officio members (three from the BNM and the secretary-general of the Treasury) and five directors drawn from the private sector.<sup>23</sup> The monarch appoints the BNM governor and the five directors from the private sector, while the minister of finance appoints the deputy governors. The governor and deputy governors are appointed for a term not exceeding five years; the directors are appointed for a term not exceeding three years. All Board members are eligible for reappointment. As stipulated in the law, the Board entrusts the BNM governor to be in charge of matters pertaining to the conduct and formulation of monetary policy.<sup>24</sup>

Among the several senior management committees, the Monetary Policy Committee (MPC), which comprises the governor, deputy and assistant governors, assesses the financial and economic developments associated with the formulation and conduct of monetary policy. The primary objective of the MPC meetings is to serve as a formal platform for comprehensive discussions on issues and developments relevant to the formulation and implementation of monetary policy. The MPC is not a decision-making committee; its role is limited to that of an internal advisory group. Rather, in setting monetary policy, the MPC ensures that the BNM Governor has the benefit of hearing various alternative opinions and perspectives before a policy decision is made.<sup>25</sup> Based on the governing legislation, the monetary policy decision remains the sole responsibility of the BNM Governor, who is accountable to the Board of Directors. The MPC receives input from the BNM's Monetary Policy Working Group, which consists of an assistant governor (acting as chairman) and other department officials. Governance and risk management procedures have also been put in place to ensure the proper running of the MPC meetings. These include a formal Terms of Reference for the MPC meeting and the strict adherence to the Central Bank's Information Security policy.

The BNM closely coordinates with other government ministries. Much of this interaction takes place through the National Economic Action Council and the Macroeconomic Inter-Agency Planning Group (one of many inter-departmental committees) that meet regularly to coordinate fiscal and monetary policy responses across agencies.<sup>26</sup> The group consists of representatives from the Ministry of Finance, the BNM, the Economic Planning Unit, and the National Economic Action Council. In the past, commentators have stated that the Ministry of Finance is perceived to be too closely involved with monetary policy-making. However, the BNM has asserted that this relationship represents an integral part of its advisory function to the government.<sup>27</sup>

### **Advance meeting schedule**

The Monetary Policy Committee meets eight times a year at predetermined intervals while the calendar of meetings is only disclosed internally. Minutes or reports of these meetings are not publicly available.<sup>28</sup> However, statements about the main considerations guiding monetary policy are made available through the central bank's Annual Report and the *Monetary Policy Statement*, the latter being published quarterly since August 2003. In addition, the senior management of the central bank, including the governor, engages in a Question & Answer session during the release



of the quarterly GDP data with the press on issues related to the economy, in particular on issues that led to the formulation of the *Monetary Policy Statement*.

## Public statements on monetary policy

### Periodic publications

The BNM issues press releases on its website announcing changes in monetary policy, the OPR, and the range and settings of monetary instruments. These provide the rationale for changes and the time span for implementation. BNM officials regularly make statements about monetary policy in speeches, many of which can be found on the central bank's website. Upon the release of the BNM *Annual Report*, the governor holds explanatory briefings for the various stakeholders, including foreign ambassadors, analysts, business chambers, and Malaysian government officials.

Malaysia's central bank releases a variety of regular publications.<sup>29</sup> The *Monthly Statistical Bulletin* contains updated information on monetary and financial aggregates and includes the BNM's and banking institutions' updated statements of assets and liabilities. Data on certain financial intermediaries, including the Employees Provident Fund and the National Savings Bank as well as updated data on financial markets and national accounts are also provided.

The quarterly *Monetary Policy Statement*, released to coincide with the announcement of GDP data, contains the central bank's analysis of macroeconomic indicators and the direction of policy intent. Between the fixed scheduled dates, additional monetary policy statements would be issued if a policy change were warranted. The publication of the *Monetary Policy Statement* coincides with the release of the quarterly GDP data and complementary analysis on the country's economic performance.

The fortnightly *Reserves Statement* describes the state of the country's foreign exchange reserves. Additional GDP statistics and data on federal government debt are found in the *Quarterly Bulletin*, which provides statistics and analysis on economic, monetary, and financial developments, as well as special features on specialised topics.

The BNM *Annual Report* provides a detailed sectoral breakdown of the Malaysian economy and a description of monetary and fiscal developments. It includes all BNM annual accounts, and the annexe provides information on foreign exchange administration policies, funds administered by the BNM, and a list of licensed banking institutions. In addition, the report includes performance and developments of the financial sector. The public can also view developments in the financial markets as well as the payment and settlement systems and external relations in the report.

The central bank also publishes books that outline the developments in the financial system involving the central bank. For example, 'The Central Bank and the Financial System "A Decade of Change"', 'Bank Negara Malaysia – The First 25 Years', and 'Money and Banking and Central Banking in an Era of Change – Landmark Speeches: 1959 – 1988'.

The BNM's liquidity forecasts and monetary operations are released daily to major commercial information service providers including Reuters, Moneyline Telerate, and Bloomberg.<sup>30</sup>

The 10-year *Financial Sector Master Plan* outlines the central bank's long-term strategy and vision for the financial sector.

The central bank also publishes occasional and discussion papers, a variety of consumer education booklets, and the *Takaful Annual Report* and the *Insurance Annual Report*, both of which deal with the insurance industry.

### **Public hearings**

The BNM is not required by law to hold public hearings before major changes to monetary policy or supervisory regulation, but it holds consultations with the private sector on a variety of monetary and regulatory issues.<sup>31</sup> In addition, after the release of the BNM *Annual Report*, the governor holds a series of briefings for various stakeholders, including foreign ambassadors, financial analysts, chambers of commerce, and government officials.

### **Regulations on data reporting by financial institutions to the central bank**

The Banking and Financial Institutions Act 1989 (BAFIA) provides for financial institutions' data reporting to the central bank. This law and subsequent regulations require both banking institutions and selected non-bank financial institutions (such as discount houses) to submit information to the BNM. The regulations are reviewed from time to time to enable the BNM to undertake its supervisory and surveillance function more effectively as well as to ensure the relevance of regulations. Since the 1997-98 financial crisis, the BNM has issued new circulars tightening some of the reporting requirements.

The Development Financial Institutions Act of 2002 (DFIA) has strengthened reporting requirements for the six Development Financial Institutions (DFIs) governed by the law. Under the DFIA, the central bank is responsible for monitoring the activities and financial performance of these institutions. The DFIs are required to submit their monthly reports and financial indicators to the BNM as part of the supervisory process. The central bank also conducts off-site surveillance and regular examinations of the DFIs using the risk-based supervision approach, which covers the effectiveness of internal audit functions, financial analysis, and the examination of information systems.<sup>32</sup>

In 1998, the BNM relaxed the definition of a non-performing loan from the international standard of three months of no interest paid to six months, although the new definition applies only to loans with repayment periods of three months or less.<sup>33</sup> Banking institutions with more stringent rules may adopt the existing three-month classification rule. Industry numbers on non-performing loans calculated using both the three-month classification and the six-month classification rules are published in the *Monthly Statistical Bulletin* and *Annual Report*.

A copy of *Guidelines for Financial Institutions* can be purchased from the central bank.

### 3. PUBLIC AVAILABILITY OF INFORMATION ON MONETARY POLICY

●●●● Compliance in progress

#### Release of central bank data

As one of the first subscribers to the IMF Special Data Dissemination Standard (SDDS), the central bank meets most of the SDDS specifications for coverage, periodicity and timeliness.<sup>34</sup> Malaysia has taken the flexibility option for the timeliness on reporting the country's international investment position (IIP), allowing for a lag of more than three quarters.<sup>35</sup> The IIP data for 2003 was released at end-2004; a lag of four quarters. Efforts are being made to release the data in a more timely fashion.<sup>36</sup>

An advance release calendar is available on the BNM's website, which provides the expected release dates for data described in the IMF's Dissemination Standards Bulletin Board (DSBB). The Department of Statistics publishes advance release calendars one quarter in advance in its *Quarterly National Product and Expenditure Accounts*.

For data with IMF-prescribed deadlines, the BNM announces the actual release dates at least one week prior to the release of the data through its website. As specified in the SDDS' *Detailed Disclosure of International Reserves Requirement*, the BNM provides additional information on international reserves, including forward-looking information on likely inflows/outflows for the next twelve months.

#### The central bank balance sheet

The BNM releases its analytical accounts on a monthly basis (within one month after the end of the reference month) in the *Monthly Statistical Bulletin*. This bulletin also provides a brief description of overall liquidity operations as part of the monthly balance sheet. In accord with Section 47 of the CBA, the central bank also publishes fortnightly *Statements of Assets and Liabilities*.<sup>37</sup> Information concerning the value of the BNM's shares in other institutions is not publicly disclosed by the BNM, but the information is usually made available in the respective institution's report. An analytical breakdown of the BNM's official reserve assets is published bi-weekly and is available on the BNM's website. There are no plans to report data on gross international reserves on a weekly basis.

#### Lender of last resort

The CBA and the Banking and Financial Institutions Act 1989 specify the BNM's capability as lender of last resort. Section 42 of the CBA provides the BNM with emergency powers to lend money or provide advances to financial institutions, in order to safeguard monetary stability and financial system viability. Section 73 of the BAFIA enables the BNM to intervene at times of emerging strains in banks and take control of insolvent banks. Furthermore, the Emergency (Essential Powers) Act 1979 and Essential (Protection of Depositors) Regulations 1986 strengthen the BNM's supervisory powers in accordance with its lender of last resort operations.

Instead of issuing emergency loans to individual banks, during the Asian financial crisis (1997-98) the BNM established Danamodal -- a separate company with its own governing body that was fully owned by the BNM. Danamodal was a special purpose vehicle to raise funds through the sale of its bonds in the domestic market to inject funds into troubled local financial institutions. Danamodal was given board-level representation in these institutions,

thus enabling it to implement reforms and facilitate a mergers programme.<sup>38</sup> Danamodal has ceased operations since December 2003, after having successfully redeemed its bonds in October 2003.

The government's blanket guarantee for deposits in Malaysia has been replaced by an explicit but limited deposit insurance scheme. The Malaysia Deposit Insurance Corporation (MDIC) Act 2005 was enacted on 15 August 2005. The MDIC Act has established the Malaysia Deposit Insurance Corporation to administer the act and the country's deposit insurance scheme. The MDIC Act allows for the system to be administered in the least costly manner, which should minimise costs to the financial system. The MDIC's membership consists of licensed banks, licensed finance companies and licensed Islamic banks. Its coverage, among others, is up to RM 60,000 per depositor per member institution. One of its features is that it covers Islamic deposits as well as conventional deposits separately up to RM 60,000 each, even when held at the same financial institution. In addition, the MDIC is also mandated to undertake the resolution of problematic banking institutions, as may be required by the BNM. On 1 September 2005, the MDIC commenced its operations.

## Public information services

The BNM has a comprehensive website that stores statistical outputs, press releases and speeches (from 1996 onwards), all available in English and Malay. The website also provides details on how local and overseas clients can purchase publications, with a price list of available documents. The latest issue of each major document (*Monthly Statistical Bulletin*, *Quarterly Bulletin*, *Annual Report*) is freely available on the website. Past issues of the *Monthly Statistical Bulletin* are also available on the website, while those of the *Quarterly Bulletin* and *Annual Report* can be purchased.

The range of publications is extensive, including historical works, occasional research papers, and detailed information sources on all areas of BNM supervision -- from Islamic banking to the Takaful industry. Visitors to the BNM, with authorisation, can also use the library to look up specific legislation, circulars, and Gazettes, often only summarised or not mentioned on the website. On 25 February 2005, the Bank Negara Malaysia Laman Informasi Nasihat dan Khidmat (LINK) was launched; its aim is to enhance the effectiveness of the BNM's interface with the public.<sup>39</sup> Bank Negara Malaysia LINK is established as a centralised point of contact with the public on issues that relate to the BNM's operations, policies, the financial sector and consumer education in the area of finance through face-to-face customer service to walk-in visitors with general enquiries or complaints.

There is also publicly available information on bills and bonds traded in Malaysia and information on the primary issues of all instruments (securities and non-securities) approved by the BNM and/or relevant authorities which are either issues on tender or on private placement via the system known as RMbond (Ringgit Bond Market) and FAST (Fully Automated System for Issuing/Tendering).<sup>40</sup> The transparency of information provided by the system facilitates both the primary and secondary market activities in the domestic bond market.

A user-friendly and informative public portal on foreign exchange administration is also available through the BNM website to provide easy access to information on the latest updates and current policies, as well as to facilitate online submission of applications and reports.

As part of the OPR framework, the central bank will continue to monitor the lending rates charged by banking institutions and, to ensure fair and just pricing, parallel measures are in place to safeguard customer interests. These include prescribing minimum disclosure standards for banking institutions to provide information on their products and services, such as information relating to lending rates, fees and charges, as well as information on the risks associated with specific financial products and services. This system will be reinforced by a ten-year consumer education programme and strengthened surveillance of the financial sector by the BNM.

## 4. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY BY THE CENTRAL BANK

●●●● Compliance in progress

### Accountability before a designated public authority

Under the Central Bank Act, the annual accounts -- certified by the Auditor General -- as well as a report by the BNM board on all annual central bank operations, are presented to the Senate and the House of Representatives. Once the BNM accounts are tabled in the parliament, the Public Accounts Committee of the Parliament (PAC) can require BNM officials to attend and answer questions and issues raised on BNM's operations and administration.

Since independence in 1957, Malaysia has been ruled by a one-party coalition, with the minister of finance coming from the dominant party, the United Malays National Organisation (UMNO). Hence, relations between the central bank and the government are largely based on relations between the prime minister, the BNM, and the minister of finance, with little explicit role for parliament. The BNM has never exercised its right to appeal to parliament over monetary policy disputes with the minister of finance. Central bank officials noted that the BNM officially reports to the minister of finance twice a year (with around six-month intervals).<sup>41</sup> Legally, under section 34(1) of the CBA, the Board of Directors is expected to keep the minister of finance informed of monetary and banking policy, and of policies under the laws that the BNM administers which the BNM pursued or intends to pursue.

### Financial statement

#### Audited financial statement

As required by law, the BNM publishes its annual financial statements within three months of the end of its financial year, which follows the calendar year. The accounts include a summary of the BNM's contingent liabilities. Section 48 of the CBA requires the accounts to be certified by the Auditor General and published in the *Government Gazette*. The accounts must be sent to the minister of finance, who presents them along with the *Annual Report*, to both the House of Representatives and the Senate.<sup>42</sup> Malaysian National Accounting Standards, Malaysian generally accepted principles of accounting, and Government Circulars guide the BNM's financial reporting framework.<sup>43</sup>

#### External and internal audit

The BNM has appropriate internal governance procedures to ensure the integrity of its operations; these are established by the Board of Directors. The BNM's Internal Audit Department, under the purview of an Internal Audit Committee of the BNM Board, enforces internal governance procedures and, in concurrence with the National Audit Department (Jabatan Audit Negara), reviews all reports. The membership of the Internal Audit Committee comprises three independent members of the Board of Directors, and it meets once every three months to review the central bank's financial operations, its internal controls, the Internal Auditor's audit programme, the performance and findings of the Internal Audit Department, and to recommend any remedial actions on the findings.<sup>44</sup>

Article 106 of the constitution and the Audit Act 1957 accords the Auditor General (Ketua Audit) with independence, whereby the institution is only accountable to the legislature. A summary of findings by the Auditor General in the BNM's financial statements is provided in the *Auditor General's Report on the Federal Statutory Bodies* for each fiscal year.<sup>45</sup>

## **Conduct of officials**

Sections 9-11 of the CBA specify procedures for the appointment and removal of the governor, deputy governor and other members of the Board of Directors. The monarch may terminate the appointment of the governor or any of the directors, and the minister of finance, and that of the deputy governors, under the conditions specified in Section 11 (2) of the CBA.<sup>46</sup>

The Public Authorities Protection Act 1948 does not prevent legal action being taken against public officials, but it shortens the limitation period for bringing lawsuits. Section 114 of the Banking and Financial Institutions Act 1989, Section 117 of the Development Financial Institutions Act 2002, and Section 77 of the Anti-Money Laundering Act 2001 legally protect BNM officers. These sections do not prevent persons from bringing lawsuits, but state that no legal process can be taken against persons for an act performed pursuant to the relevant legislation and carried out in good faith.

The CBA details the legal responsibilities of the governor, directors, and general staff, including the disclosure and/or processes concerning conflicts of interests. BNM officers are required to wait six months prior to joining any financial institution after leaving the central bank; this requirement is based on the guidelines issued by the BNM's Human Resources Management Department in 1995. BNM officers are legally proscribed from revealing information gained from their professional duties, except when exercising their duties or when required to do so by a court or law. The BNM can report suspected offences by its own members and supervised institutions to the relevant authorities.

## INTERVIEWS

Representatives of *Oxford Analytica* interviewed the following individuals during a visit to Malaysia between 7 and 10 November 2005:

### Bank Negara Malaysia

#### 9 November 2005

Sukhdave Singh	Director	Monetary Assessment and Strategy Dept.
Thomas Koon Peng Tan	Manager	Monetary Assessment and Strategy Dept.

### Ministry of Finance

#### 10 November 2005

Yeo Heng Hau	Deputy Secretary	Economic and International Division
Chua Tong Ka	Head Fiscal Section	Economic and International Division
Mohd. Reezal bin Ahmad		Economic and International Division
Ahmad Fareedzal bin Abu Bakar		Economic and International Division
Nik Mohd. Shariffudin Nik Hassan		Economic and International Division
Fauziah binti Yaacob		Budget Management Division
Noor Aliza binti Mohd. Shaffi		Budget Management Division
Kong Hee Eng		Financial Management Advisory Division
Ismail bin Hj Bakar		Government Procurement Division
Ahmad Fauzi bin Sungip		Government Procurement Division
Mohd. Azmi Mazid Mohd. Yazid		MoF (Inc) and Privatisation Division
Isma Juwana Ab. Aziz		Monitoring and Control Division
Ooi Eng Chor		Monitoring and Control Division
Khodijah Bt. Abdullah		Tax Analysis Division

### Economic Planning Unit, Prime Minister's Department

Yap Siew Hong	Director	Macroeconomics Section
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## ADDITIONAL INTERVIEWS

#### 7 November 2005

Dato' Param Cumaraswamy	President	Transparency International Malaysia
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#### 8 November 2005

R. Thillainathan	Executive Director and COO	Genting Corporation
Azidin Wan Abd. Kadir	Research Fellow	Malaysian Institute of Economic Research



## NOTES

<sup>1</sup> The Central Bank of Malaysia Act 1958 (Revised 1994) is available at:

[www.bnm.gov.my/index.php?ch=14&pg=17&ac=13&full=1](http://www.bnm.gov.my/index.php?ch=14&pg=17&ac=13&full=1)

<sup>2</sup> Written comments from Bank Negara Malaysia to *Oxford Analytica*, 24 November 2003, p.5.

<sup>3</sup> See the Bank Negara Malaysia publications *Central Banking in an Era of Change: Landmark Speeches, 1959-1988* and *The Central Bank and the Financial System in Malaysia: A Decade of Change, 1989-1999*.

<sup>4</sup> See press statements section at: [www.bnm.gov.my/index.php?ch=107](http://www.bnm.gov.my/index.php?ch=107)

<sup>5</sup> Interviews in Malaysia, 20-24 October 2003 and 7-10 November 2005. For example, PM Abdullah Badawi said that “[the government] don’t fiddle and tinker with interest rates. We leave it entirely to the central bank.” after BNM raised the key overnight policy rate by 30 basis points to 3%; the first hike in seven years. See ‘Malaysia PM: Ctrl Bank, Not Govt to Decide Rate Hikes’, Dow Jones Newswires, 2 December 2005.

<sup>6</sup> Section 34, Central Bank of Malaysia Act 1958 (Revised 1994).

<sup>7</sup> Written comments from Bank Negara Malaysia to *Oxford Analytica*, 27 September 2004, p. 4.

<sup>8</sup> Interviews in Malaysia, 20-24 October 2003.

<sup>9</sup> In September 2002, Dr. Mahathir criticised banks for not lending enough and hinted that the statutory reserve requirement ratio may be raised if banks did not increase their loans. See Alice Chia, ‘Be project-minded, local financial institutions told’, *Business Times*, 6 October 2002.

<sup>10</sup> Interviews in Malaysia, 20-24 October 2003.

<sup>11</sup> Section 30 (ffff), Central Bank of Malaysia Act 1958 (Revised 1994).

<sup>12</sup> Interviews in Malaysia, 7-10 November 2005.

<sup>13</sup> Interviews in Malaysia, 7-10 November 2005. The Board of Directors oversees the policy and general administration of the affairs and business of the BNM as provided in section 8 (1) of the CBA. Hence, the PPAP would fall within the purview of the powers of the Board of Directors. Besides this, the PPAP would also be subject to section 14 of the CBA, where a director (of the Board of Directors) is required to disclose his vested interests (if any) in a contract made or proposed to be made by the BNM and to abstain from any deliberation or decision with respect to it.

<sup>14</sup> Written comments from Bank Negara Malaysia to *Oxford Analytica*, 3 November 2004, p. 1.

<sup>15</sup> Interviews in Malaysia, 7-10 November 2005. Central bank officials have emphasised that the BNM acts independently on the profit allocation decision and then makes the necessary recommendation to the minister of finance.

<sup>16</sup> Section 7, Central Bank of Malaysia Act 1958 (Revised 1994).

<sup>17</sup> Interviews in Malaysia, 20-24 October 2003.

<sup>18</sup> See ‘BNM introduces new interest rate framework’ PEN: 04/04/34 (BNM press release) at:

[www.bnm.gov.my/index.php?ch=8&pg=14&ac=831](http://www.bnm.gov.my/index.php?ch=8&pg=14&ac=831)

<sup>19</sup> Interviews in Malaysia, 7-10 November 2005.

<sup>20</sup> See ‘Malaysia Adopts a Managed Float for the Ringgit Exchange Rate’, BNM press release 21 July 2005 at:

[www.bnm.gov.my/index.php?ch=8&pg=14&ac=1054](http://www.bnm.gov.my/index.php?ch=8&pg=14&ac=1054)

<sup>21</sup> Interviews in Malaysia, 7-10 November 2005. The ringgit exchange rate is connected to a basket of currencies, but there is no transparency in the composition of the basket or the weights given to the various currencies in the basket. This lack of disclosure should help the BNM fend off ‘hot money’ speculators, which could profit from increased volatility of the ringgit against a particular currency, and thus prompting the central bank to conduct additional foreign exchange transactions that would otherwise be unwarranted.

<sup>22</sup> Section 19, Central Bank of Malaysia Act 1958 (Revised 1994).

<sup>23</sup> Section 8, Central Bank of Malaysia Act 1958 (Revised 1994) provides for the composition of the BNM’s Board of Directors. The Board of Directors should consist of the governor, not more than three deputy governors and not fewer than five but no more than eight directors appointed under the requirements of Section 10.

<sup>24</sup> Interviews in Malaysia, 27 September – 1 October 2004.

<sup>25</sup> Interviews in Malaysia, 7-10 November 2005.

<sup>26</sup> Interviews in Malaysia, 20-24 October 2003.

<sup>27</sup> Interviews in Malaysia, 27 September – 1 October 2004 and 7-10 November 2005.

<sup>28</sup> Interviews in Malaysia, 7-10 November 2005. The MPC is not a decision-making committee and its role is limited to that of an internal advisory group. Based on the governing legislation, the monetary policy decisions remains the sole responsibility of the BNM Governor, who is accountable to the Board of Directors. Monetary policy decisions are thus not reached through a formal voting procedure.



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<sup>29</sup> See 'Publications' at: [www.bnm.gov.my/index.php?ch=11](http://www.bnm.gov.my/index.php?ch=11)

<sup>30</sup> Interviews in Malaysia, 27 September – 1 October 2004. This information is provided to enhance transparency in the implementation of monetary policy.

<sup>31</sup> Interviews in Malaysia, 20-24 October 2003.

<sup>32</sup> Written comments from Bank Negara Malaysia to *Oxford Analytica*, 24 November 2003, p.10.

<sup>33</sup> Interviews in Malaysia, 20-24 October 2003. Written comments from Bank Negara Malaysia to *Oxford Analytica*, 24 November 2003, p.11.

<sup>34</sup> See Economic and Financial Data for Malaysia at: [www.bnm.gov.my/index.php?ch=111](http://www.bnm.gov.my/index.php?ch=111)

<sup>35</sup> See IMF SDDS website at: <http://dsbb.imf.org/>

<sup>36</sup> Interviews in Malaysia, 27 September – 1 October 2004. As part of these efforts, the BNM is overseeing a review of the Department of Statistics, focusing on its efficiency.

<sup>37</sup> See the BNM Statement of Assets & Liabilities at: [www.bnm.gov.my/index.php?ch=12&pg=142](http://www.bnm.gov.my/index.php?ch=12&pg=142)

<sup>38</sup> *Danamodal's* representation in each institution's Board of Directors reduced as the capital injection was repaid.

<sup>39</sup> Interviews in Malaysia, 7-10 November 2005. See [www.bnm.gov.my/bnmlink/](http://www.bnm.gov.my/bnmlink/)

<sup>40</sup> See RMbond at: <http://rmbond.bnm.gov.my/> and FAST at: <https://fast.bnm.gov.my/fastweb>

<sup>41</sup> Interviews in Malaysia, 1-5 November 2002.

<sup>42</sup> Section 48, Central Bank of Malaysia Act 1958 (Revised-1994). See Certificate of the Auditor General, Chapter 13 – Annual Accounts, 2004 Annual Report at:

[www.bnm.gov.my/files/publication/ar/en/2004/ar2004.complete.pdf](http://www.bnm.gov.my/files/publication/ar/en/2004/ar2004.complete.pdf)

<sup>43</sup> Accounting standards in Malaysia are based on International Accounting Standards (IAS), and are reflective of International Generally Accepted Accounting Principles (IGAAP). The Malaysian Accounting Standards Board (MASB) is an independent authority to develop and issue accounting and financial reporting standards in Malaysia. See: [www.masb.org.my/masbstd\\_smry.htm](http://www.masb.org.my/masbstd_smry.htm)

<sup>44</sup> Interviews in Malaysia, 7-10 November 2005.

<sup>45</sup> See Badan Berkanun Persekutuan Tahun 2004 report (in Bahasa Malaysia only) at:

[www.audit.gov.my/BM/Laporan\\_KAN/Laporan%20BBP%202004.pdf](http://www.audit.gov.my/BM/Laporan_KAN/Laporan%20BBP%202004.pdf)

<sup>46</sup> Specified conditions include: if the official resigns, becomes of unsound mind or incapable of carrying out his duties, becomes bankrupt, is convicted by a court of law of any offence involving dishonesty, is guilty of serious misconduct in relation to his duties, is absent (except on leave granted by the minister of finance) from all meetings of the board held during two consecutive months or during any three months in any period of twelve months, or fails to disclose to the Board a potential situation of conflict of interests and did not abstain from deliberating and deciding on a matter which he is interested in.